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IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED : 8.2.2006

CORAM :

THE HONOURABLE MR.JUSTICE P.D.DINAKARAN
AND
THE HONOURABLE MR.JUSTICE P.P.S.JANARTHANA RAJA

Tax Case (A) No.58,59,96 & 97 of 2006
and T.C.M.P.Nos.46 & 82 of 2006

Commissioner of Income Tax
Madurai ...Appellant in all the cases

-Vs-

M/s.L.S.Mills Ltd.,
Madurai Road,
Theni ... Respondent in all the appeals.

Prayer: Appeals filed under Section 260-A of the Income Tax Act 1961 against the orders of the Income Tax Appellate Tribunal Madras 'C' Bench, Chennai dated 23.6.2005 and 26.4.2005 in I.T.A.Nos. 433, 434, 190, 220,/Mds/2001 for the assessment years 1993-94, 95-96, 1996-97 and 1995-96 respectively.
Against the order of the Commissioner of Income Tax (Appeals) XIII, Chennai dated 5.12.2000 made in I.T.A.Nos.454/1999-2000 and 437/1999-2000 respectively against the order of the the Deputy Commissioner of Income Tax, Special Range II, Madurai dated 4.3.98 and made in P.A.N. / G.I.R. No. 49-003-Cz-8024 for the Assessment year 1993-94 and 1995-96 respectively (T.C.58 and 59 of 2006)

against the order of the Commissioner of Income tax (Appeals) Madurai dated 13.12.2000 made in I.T.A.No.217-99-2000 against the order of the Deputy Commissioner of Income tax, Special Range II, Madurai dated 4.3.1998 made in P.A.N/G.I.R.No.49-003-C2-8024 for the Assessment year 1995-96 (T.C.96/2006)

against the order of the Commissioner of Income Tax (Appeals) XIII, Chennai-34 dated 5.12.2000 made in G.T/Appeal No. 454/199-2000 against the order of the Deputy Commissioner of Income Tax, Special Range -II, Madurai dated 31.3.1999 and made in P.A.N/G.I.R. No. 49-003-C2-8024 for the Assessment year 1996-97 (T.C. 97/2006)

For Appellant : Mr.Narayanaswamy Standing Counsel

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O R D E R

(Order of the Court was made by P.D.DINAKARAN, J.)

Heard. The above appeals are preferred under Section 260-A of the Income Tax Act 1961 against the orders of the Income Tax Appellate Tribunal Madras Bench "C" dated 23.6.2005 and 26.4.2005 in I.T.A.Nos. 433, 434, 190, 220,/Mds/2001.

2. The facts in brief are : The assessee company is a private limited company engaged in the manufacture and sale of yarn. For the assessment years 1993-94, 1995-96, 1996-97 and 1995-96, the assessing officer, disallowed the claim of the assessee in respect of replacement of old machinery by new one on the ground that the same cannot be treated as a revenue expenditure; treated the MODVAT credit relating to the replacement of machinery as capital; recalculated the benefit under Section 80 HHC by including the excise duty and sales tax to the total turnover and also disallowed the excess remuneration paid to the director. Aggrieved by the said order, the assessee filed appeals before the CIT(Appeals). The Commissioner of Income Tax(appeals), allowed the above issues in favour of the assessee. Aggrieved by the same, the Revenue filed appeals before the Income Tax Appellate Tribunal. The Appellate Tribunal dismissed the appeals filed by the Revenue.

3. Aggrieved by the said order of the appellate Tribunal, the Revenue has filed T.C.Nos.58 & 59 of 2006 by raising the following substantial questions of law:-

1. Whether in the facts and circumstances of the case, the Tribunal was right in law in holding that the expenditure incurred by the assessee during the accounting year on the replacement of machinery was deductible as current repairs/revenue expenditure?

2. Whether on the facts and in the circumstances of the cae, the appellate Tribunal was right in law in holding that addition made on account of MODVAT credit relating to the machinery is a revenue expenditure.

3. Whether in the facts and circumstances of the case, the Tribunal was right in holding that sales tax and excise duty does not form part of the turnover, for the purpose of calculation of deduction u/s.80 HHC?

4. Whether on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in holding that the excess remuneration paid to the Directors is allowable as a deduction?

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and filed T.C.Nos.96 and 97 by raising the following substantial question of law:

> "Whether on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in holding that the excess remuneration paid to the Directors is allowable as a deduction?"

4. It is fairly conceded by the learned counsel appearing for the Revenue that the issue involved in question No.1 in T.C.Nos.58 and 59 of 2006 is covered by the decision of this Court rendered in COMMISSIONER OF INCOME TAX VS. JANAKIRAM MILLS LTD. (275 ITR 403), the issue involved in question No.2 is covered by the decision of the Supreme Court in COMMISSIONER OF INCOME TAX VS. INDO NIPPON CHEMICALS CO.LTD.(261 ITR 275) and the third question is covered by the decision of this Court rendered in the COMMISSIONER OF INCOME TAX VS. WHEELS INDIA LTD. (275 ITR 319).

5.1. With regard to the first question, the replacement of machinery is capital or revenue is not determined by the treatment given in the books of account or in the balance sheet. The claim has to be determined only by the provisions of the act and not by the accounting practice of the assessee. In the instant case, the Commissioner and the Appellate Tribunal, finding that replacement of machinery is a revenue expenditure, held that the claim of the assessee cannot be disallowed as the said replaced machinery did not bring about any asset or any distinct advantage to the assessee and no structural change was also brought in.

5.2. This Court, in the decision first cited supra in the COMMISSIONER OF INCOME-TAX v. JANAKIRAM MILLS LTD. (2005) (275 ITR 403), held that all plant and machinery put together amount to a complete spinning mill which is capable of manufacturing yarn and hence, each replaced machine could not be considered as an independent one and no intermediate marketable product was produced.

5.3. Hence, first question in T.C.Nos.58 and 59 of 2006 is answered against the Revenue.

6.1. With respect to the second question in T.C.Nos.58 and 59 of 2006 viz., the addition made on account of MODVAT credit relating to the machinery is a revenue expenditure, admittedly, the MODVAT credit relates to replacement of machineries. Since the cost of replacement was allowed as revenue expenditure, addition made on account of MODVAT credit relating to the machinery is a revenue expenditure.

6.2. The Supreme Court in the decision second cited supra

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viz., COMMISSIONER OF INCOME TAX VS. JANAKIRAM MILLS LTD. (275 ITR 403), held that merely because the MODVAT credit was an irreversible credit available to manufacturers upon purchase of duty-paid raw materials, that would not amount to income which was liable to be taxed under the Act; income was not generated to the extent of the MODVAT credit on unconsumed raw material.

6.3. Hence, second question in T.C.Nos.58 & 59 of 2006 is answered against the Revenue.

7.1. With respect to the third question in T.C.Nos.58 & 59 of 2006 viz., whether the excise duty and sales tax should be excluded from the total turnover for the purpose of deduction under Section 80HHC, the Tribunal, following the decision rendered by this Court in The Commissioner of Income Tax vs. Madras Motors Ltd. (257 ITR 60) confirmed the order of the Commissioner of Income Tax (Appeals) in directing the Assessing Officer to exclude the excise duty and sales tax from the total turnover.

7.2. This Court in the decision third cited supra in the COMMISSIONER OF INCOME TAX VS. WHEELS INDIA LTD. (275 ITR 319), held that it is highly impossible to accept the contention that the term 'turnover' would include the excise duty and sales tax components which are all indirect taxes and which the assessee has to collect and pay over to the Government and such statutory dues will not have any element of profit of business and therefore, the Sales tax and excise duty are not to be included in the total turnover while computing the deduction under Section 80HHC.

7.3. Hence, question No.3 in T.C.Nos.58 & 59 of 2006 is answered against the Revenue.

8.1. As far as the fourth question in T.C.Nos.58 and 59 of 2006 and the only question in T.C.Nos.96 and 97 of 2006 viz., the excess remuneration paid to the directors is allowable as a deduction is concerned, the assessing officer disallowed a sum of Rs.16,29,000/- being the excessive remuneration paid to the Directors. The details of the payment of remuneration to the Directors are as under:

Shri L.S.Manivannan	Rs.6,08,250
Shri L.S.Prabhakaran	Rs.6,08,250
Smt.Shanthi Manivannan	Rs.6,08,250
Smt.usha Devi	Rs.6,08,250

the Assessing Officer restricted the claim of payment of remuneration to the first two Directors at Rs.25,000/- per month and payment to the two lady Directors at Rs.8,500/- per month. Accordingly excess claim was disallowed as under:-

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Name of the Director	Remuneration	Allowable	Disallowance
Shri L.S.Manivannan	Rs.6,08,250	300000	308250
Shri L.S.Prabhakaran	Rs.6,08,250	300000	308250
Smt.Shanthi Manivannan	Rs.6,08,250	102000	506250
Smt.usha Devi	Rs.6,08,250	102000	506250

the assessing officer disallowed a sum of Rs.16,29,000/- out of the total payment of remuneration to the Directors. Aggrieved by that order, the assessee filed appeals to the Commissioner of Income Tax (Appeals), who, after looking into the issues, has come to the conclusion that the salary paid to the lady Directors was excessive dictated by non-business consideration. Accordingly, he had given directions that monthly salary of Rs.15,000/- would be a reasonable proposition in view of the services that would have been totally rendered and directed the assessing officer to allow the claim of payment of salary to the first two directors and to restrict the payment of salary to lady Directors at Rs.15,000/- per month. Accordingly, the appellant got relief of Rs.7,72,500/-.

8.2. Aggrieved by the said order, the Revenue filed appeals to the Income Tax Appellate Tribunal, which, considering the factual situation, allowed the claim of the assessee and dismissed the Revenue appeal.

8.3. It could be seen that both the authorities below had concurrently given finding that these Directors have rendered services. Hence, disallowance made by the assessing officer towards the remuneration payable to the Directors is not fair. That apart, the learned standing counsel appearing for the Revenue, did not place any material to show that the remuneration was excessive. When there is a factual finding that the remuneration paid by the assessee to its Directors is reasonable, we find no error or infirmity in the order of the Appellate Tribunal.

8.4. Hence, question No.4 in T.C.Nos.58 & 59 of 2006 and the only question in T.C.Nos.96 & 97 of 2006 is answered against the Revenue.

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9. In view of the foregoing conclusion, we do not find any error in the orders of the Tribunal and no question of law much less a substantial question of law arises for consideration of this Court. Hence, the appeals are dismissed. Consequently, connected T.C.M.Ps. are dismissed.

Sd/-
Asst. Registrar.

/true copy/

Sub Asst. Registrar.

msk

To

1.The Assistant Registrar,Income Tax
Appellate Tribunal, Madras Bench "C". Bench
Rajaji Bhavan, Besant Nagar, Chennai-90.

2.The Commissioner of Income Tax
(Appeals) XIII, 121, Mahatma Gandhi
Road, Chennai-600 034.

3.The Deputy Commissioner of Income-tax,
Spl. Range II, Madurai

4.The Commissioner of Income Tax, Madurai.

2 ccs to Mrs.Pushya Sitaraman, Advocate, Sr. 5763, 5773

T.C.(A)Nos.58, 59,
96 & 97 of 2006

VC (CO)
kk 17/3

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